IDAHO OUTLOOK

NEWS OF IDAHO'S ECONOMY AND BUDGET

STATE OF IDAHO **DIVISION OF FINANCIAL MANAGEMENT** **JANUARY 2008 VOLUME XXX NO. 7**

Financial market turmoil has shifted policymakers into high gear. Within a week, monetary and fiscal stimulation policies have been developed. It started on January 21, 2008. It was a bad day, even for a Monday. Every major foreign stock index declined. That day's losses ranged from a high of 7.4% for India's BSE 30 and Russia's RTS to a low of 3.9% for the Japanese Nikkei Stock Index. Germany's DAX dropped 7.2%, the U.K.'s FTSE 100 fell 5.5%, and China's Shanghai SE retreated 5.1%. These declines raised fears the U.S. stock market, which was idle for the Martin Luther King, Jr. holiday on Monday, would also fall when trading resumed on Tuesday.

What almost no one foresaw was the Federal Reserve's decision to lower its bellwether federal funds rate by 75 basis points to 3.5% on Tuesday. The Federal Reserve did not directly reference Monday's global-stock market meltdown in its press release, merely noting that "broader financial market conditions have continued to deteriorate." Instead, it emphasized the weakening prospects for U.S. economic growth. The Federal Reserve's focus makes sense. Although the global equity markets' plunge on Monday triggered the U.S. central bank's move, it was not the underlying cause. Both the Federal Reserve and financial markets are responding to the increasing risk of a U.S. slowdown and that it will pull the rest of the world down with it.

The Federal Reserve's announcement reported that "appreciable downside risks to growth still remain." This suggests the Federal Reserve will continue to loosen, which it did on January 30th, with another 50 basis point reduction. Economists at Global Insight, Inc. expect the U.S. central bank will cut another 50 basis points off its federal funds rate, which would take it down to 2.5% by late April. It appears the central bank's move has helped quell financial market fears. The Dow Jones Industrial Average closed at 11,971 on January 22nd, but had recovered to 12,443 at the close on January 30th. However, it will take longer for the rate cuts to have an impact on the economy. A general rule of thumb is there is a 9- to 18-month lag before monetary policy affects the economy.

The turmoil in the financial markets also lit a fire under fiscal policymakers this week. Congressional leaders in the House of Representatives and the White House agreed on January 24, 2008 to an economic stimulus package worth around $150 billion. There are three key elements to the plan. A $100 billion tax rebate for individuals. Any individual who earned more than $3,000 in 2007 will receive a rebate. Individuals will receive $300 and working couples will get $600. In addition, there is a $300 per child rebate for couples with children. The rebates are phased out for individuals earning over $75,000 and couples earning $150,000. The plan also includes business tax cuts worth about $50 billion. Lastly, the cap on loans purchased by government sponsored agencies Fannie Mae and Freddie Mac will be lifted from the present $417,000 limit to a cap of about $725,000. The limit on Federal Housing administration loans will be raised from $362,000 to $725,000. The Senate is now developing its own version of the stimulus plan which would add about $11 billion to the package.

The goal of the plan is to spur consumer spending via the tax rebate, increase business investment with enhanced depreciations, and boost housing by extending the conforming loan limits for government agencies. The biggest effects of the plan should come in the second half of this year, which reflects the fact the IRS will not be able to begin sending out rebate checks until May of 2008. Global Insight economists estimate the House plan will boost GDP growth in 2008 by 0.3-0.4 percentage point. This estimate will be refined as more information becomes available and the plan is finalized.

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General Fund Update

As of December 31, 2007

	$ Millions		
Revenue Source	FY08 Executive Estimate[3]	DFM Predicted to Date	Actual Accrued to Date
Individual Income Tax	1,404.2	616.9	617.3
Corporate Income Tax	184.5	79.5	76.8
Sales Tax	1,170.8	607.3	606.9
Product Taxes[1]	26.8	14.5	14.5
Miscellaneous	125.9	54.2	60.4
TOTAL GENERAL FUND[2]	**2,912.2**	**1,372.4**	**1,375.9**

1 Product Taxes include beer, wine, liquor, tobacco and cigarette taxes
2 May not total due to rounding
3 Revised Estimate as of January 2008

General Fund revenue was $3.5 million ahead of target in December, making this the sixth consecutive month of revenue above expectations in FY 2008. December is the first month under the new General Fund revenue forecast that was released with the Executive Budget. The current forecast is $6.9 million higher than the forecast released last August.

Individual income tax revenue was $0.4 million higher than expected in December. Within the components of the income tax, filing payments were $0.2 million lower than expected for the month. Withholding payments were $6.9 million higher than expected but were offset by refunds that were also $6.3 million higher than expected. Withholding collections were expected to grow 10.1% in December over the year earlier level, but actually grew by 18.5%. This appears to be due to a combination of large year-end bonuses and severance payouts. The new individual income tax forecast is $11.7 million higher than last August's forecast.

Corporate income tax revenue was $2.7 million lower than expected in December. The principal reason for December's weakness was $3.4 million less in filing collections and $3.8 million less in estimated payments than were expected. These were partially offset by refunds that were $4.6 million lower than expected. The new corporate income tax forecast is $4.6 million lower than last August's forecast.

Sales tax revenue was $0.4 million lower than expected in December, making this the third consecutive month of the fiscal year that sales tax receipts fell short of expectations. The new sales tax forecast is $1.5 million lower than last August's forecast.

Product taxes were on target in December and miscellaneous revenues were $6.2 million higher than expected in December. The bulk of December's strength ($4.5 million) was from unclaimed property receipts that tend to be quite variable in their timing. Also contributing were the insurance premium tax ($0.7 million), mine license tax ($0.5 million), and interest earnings ($0.5 million).